

FIELDS OF SPECIALIZATION

Applied Microeconomics
Econometrics
Industrial Organization
Telecommunications
Labor Economics

ARTICLES

- "Have Mergers of Large Local Exchange Carriers Led to Discrimination Against Rivals? An Empirical Investigation" July 2002 (forthcoming, ABA publication on the use of econometrics in litigation, with Dennis Carlton and Thomas Stenwede).
- "Recent Developments in U.S. Antitrust Enforcement," *The United States Antitrust Review*, October 1999 (with Gustavo Bamberger).
- "Market Power and Vertical Restraints in Retailing: An Analysis of FTC v. Toys 'R' Us," in The Role of the Academic Economist in Litigation Support, edited by Daniel Slottje (1999), with Dennis Carlton.
- "The Competitive Effects of Line-of-Business Restrictions in Telecommunications," Managerial and Decision Economics (1995), with Kenneth Arrow and Dennis Carlton. (Reprinted in R. Higgins and P. Rubin, eds., Deregulating Telecommunications: The Baby Bells' Case for Deregulation, Wiley Series in Managerial Economics, 1995.)
- "Applications of Economic Theory and Econometric Methods to Merger Review in the United States," (paper presented to European Commission Merger Task Force, 1992), with A. Rosenfield and W. Bishop.
- "Unemployment Incidence and Duration: 1968-1982," American Economic Review (June 1985).
- "The Pay Gap and Occupational Segregation: Implications for Comparable Worth," Proceedings of the Industrial Relations Research Association (1985), with June O'Neill.
- "Work-Related Accidents and the Production Process," Journal of Human Resources (Winter 1985).
- "Labor Force Participation and the Relative Earnings of Black and White Males: 1940-80," with Andy Sparks, (paper presented at the World Congress of the Econometric Society, 1985).
- "Comment on McIntyre: Estimating Long-Term Labor Market Flows from CPS Data," Proceedings: Conference on Applications of Gross Flow Data, U.S. Bureau of the Census (1985).
- "The Changing Makeup of the Military and the Effect on Labor Force Data," Monthly Labor Review (July 1984), with Cheryl Cole.

"Accuracy of Response in Labor Market Surveys: Evidence and Implications," Journal of Labor Economics (October 1983), with Wesley Mellow.

"Safety and Productivity in Underground Coal Mining," Review of Economics and Statistics (May 1983).

"Economic Incentives and Safety Regulation," American Economist (Summer 1983).

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REPORTS

The Economic Progress of Black Men in America, U.S. Commission on Civil Rights (1986).

Economic Status of Americans of Eastern and Southern European Ancestry, U.S. Commission on Civil Rights (1986).

Report of the President's Task Force on Food Assistance, Curran Press, Alexandria, Virginia (1984).

MISCELLANEOUS

University-Industry Dissertation Fellowship, University of Wisconsin, 1979-80.

Referee for:

Journal of Human Resources	National Science Foundation
Journal of Industrial Economics	Policy Studies Journal
Journal of Labor Economics	Review of Economics and Statistics
Journal of Law and Economics	Social Science Research Council
Journal of Legal Studies	U.S. Department of Health and Human Services
National Commission on Employment Policy	Antitrust Law Journal

TESTIMONIAL EXPERIENCE

Sunrise International Leasing Corporation v. Sun Microsystems, Inc., United States District Court for the District of Minnesota, No. 01-CV-1057 (JMR/FLN). Affidavit on behalf of Sun Microsystems, March 2003 (with Dennis Carlton), relating to damage issues.

Sunrise International Leasing Corporation v. Sun Microsystems, Inc., United States District Court for the District of Minnesota, No. 01-CV-1057 (JMR/FLN). Affidavit on behalf of Sun Microsystems, January 2003, relating to discovery issues.

Vitamin Antitrust Litigation, MDL No. 1285, Declaration on behalf of opt-out plaintiffs, November 2002 (with William Landes and Gustavo Bamberger), relating to niacin damage issues.

Mesler v. Prudential Insurance, et al., Circuit Court of Cook County, Illinois, No. 99 L 37, November 2002, on behalf of Prudential Insurance, et al. (Deposition testimony, January 30, 2003; March 6, 2003).

MHC Financing Limited Partnership v. City of San Rafael, United States District Court for The Northern District of California, Expert Report on behalf of MHC, September 13, 2002 (with Daniel R. Fischel); Supplemental Report, September 30, 2002.

Vitamin Antitrust Litigation, MDL No. 1285, United States District Court for the District of Columbia, deposition testimony, August 7-8, 2002, August 27, 2002, on behalf of opt-out plaintiffs.

Vitamin Antitrust Litigation, MDL No. 1285, United States District Court for the District of Columbia. Declaration on behalf of opt-out plaintiffs, August 2002 (with William M. Landes and Gustavo Bamberger), relating to present value adjustment.

Vitamin Antitrust Litigation, MDL No. 1285, United States District Court for the District of Columbia. Reply Expert Report on behalf of opt-out plaintiffs, July 2002 (with William M. Landes and Gustavo Bamberger), relating to damages.

Dean Foods, Kraft Foods, Ralston Purina Company, Nabisco, Inc. and McKee Foods v. Eastman Chemical, et al., United States District Court, Northern District of California, San Francisco Branch. Supplemental Declaration on behalf of Dean Foods, et al., June 2002.

Vitamin Antitrust Litigation, MDL No. 1285, United States District Court for the District of Columbia. Expert Report on behalf of opt-out plaintiffs, May 2002 (with William M. Landes and Gustavo Bamberger), relating to damages.

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Joint Declaration to Federal Communications Commission, GN Docket No. 00-185, in the matter of Inquiry Concerning High-Speed Access to Internet Over Cable and Other Facilities (with K. Arrow, G. Becker, D. Carlton, R. Gertner, D. Fischel, J. Kalt, and G. Bamberger), May 2002, on behalf of Verizon.

Declaration of Hal Sider in Re: Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services; Before the Federal Communications Commission, Washington DC, CC Docket No. 01-337, FCC 01-360, March 1, 2002 (with Dennis Carlton), May 2002 (with Dennis Carlton and Gustavo Bamberger), on behalf of Verizon.

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Forest Laboratories, Inc. v. G.D. Searle and Co., U.S. District Court for the Northern District of Illinois, Eastern Division, CA No. 98C-5170. Expert Report on behalf of Forest Laboratories, April 2001 (with David Gross).

Reply Declaration Re: Joint Application of Northpoint Communications and Verizon Communications for Authority to Transfer Control of Blanket Authorization to Provide Domestic Interstate Telecommunications Services as a Non-Dominant Carrier: Before the Federal Communications Commission, Washington DC, Docket No. 00-157, October 17, 2000 (with Dennis Carlton), on behalf of Verizon and Northpoint.

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Ex Parte Declaration to Federal Communications Commission, CC Docket No. 99-333, in the matter of Joint Application of MCI WorldCom and Sprint for Consent to Transfer Control, May 2000, on behalf of SBC.

Gas City, Ltd. v. Indiana Department of Transportation, Circuit Court of St. Joseph County, Indiana. Affidavit on behalf of Gas City, March 2000.

Declaration before the Federal Communications Commission, CC Docket No. 99-333, in the matter of Joint Application of MCI WorldCom and Sprint for Consent to Transfer Control, February 2000 (with Dennis Carlton), on behalf of SBC.

Ex Parte Comments to Federal Communications Commission, CC Docket No. 99-272, in the matter of the Merger of Qwest Communication International Inc. and U S WEST, February 2000, on behalf of Qwest and U S WEST.

Lemon, Myer, Duncan et al. v. International Union of Operating Engineers, et al., U.S. District Court for the Eastern District of Wisconsin, Case No. 97-C-0857. Affidavit on behalf of International Union of Operating Engineers (December 1999); deposition (January 2000); Supplemental Report (February 2000).

Declaration before the Federal Communications Commission, CC Docket No. 99-272, in the matter of Merger of Qwest Communications International Inc. and U S WEST, Inc., October 18, 1999 (with Dennis Carlton), on behalf of Qwest and U S WEST.

Ex Parte Report to the Federal Communications Commission, CC Docket No. 98-141 regarding the Merger of SBC Communications Inc. with Ameritech Corporation, April 1999 (with Dennis Carlton) on behalf of SBC and Ameritech.

Riverside Pipeline Co. v. Panhandle Eastern Pipeline Co., United States District Court for the Western District of Missouri, Case No. 97-0642-CV-W-4, Expert Report in September 1998, on behalf of Panhandle Eastern Pipeline Co.

Lemon, Myer, Duncan et. al. v. International Union of Operating Engineers, et al., United States District Court for the Eastern District of Wisconsin, Case No. 97-C-0857; Affidavit in September 1998, on behalf of International Union of Operating Engineers.

Testimony before the Department of Public Service of the State of West Virginia in the Matter of Application of WorldCom, Inc., Corp., for Approval to Transfer Control of MCI Communication to WorldCom, Inc. (June 17, 1998); oral testimony (July 2, 1998), on behalf of WorldCom.

Testimony before the Department of Public Service Regulation, Public Service Commission of the State of Montana, Docket No. D97.10.191, in the Matter of the Application of WorldCom, Inc. and MCI Communications Corporation for Approval to Transfer Control of MCI Communications Corporation to WorldCom, Inc., May 12, 1998, on behalf of WorldCom.

Testimony before the Public Utilities Commission of the State of Colorado, Docket No. 97A-494T, in re Application of WorldCom, Inc. for Approval to Transfer Control of MCI Communications Corporation to WorldCom, Inc., pre-filed direct testimony (March 25, 1998), cross-examination (April 2, 1998); on behalf of WorldCom.

Affidavit before the Florida Public Service Commission, Docket No. 971375-TP, Petition of WorldCom, Inc. for Approval to Transfer Control of MCI Communications Corporation to WorldCom, Inc., February 27, 1998 (with Dennis Carlton); on behalf of WorldCom.

Affidavit before the New York State Public Service Commission, Case 97-C-1804, Petition of WorldCom, Inc. for Approval to Transfer Control of MCI Communications Corporation to WorldCom, Inc., February 16, 1998 (with Dennis Carlton); on behalf of WorldCom.

Second Declaration before the Federal Communication Commission, CC Docket No. 97-211, in the Matter of Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc., March 19, 1998 (with Dennis Carlton); on behalf of WorldCom and MCI.

Shuller v. United States, U.S. District Court for the Eastern District of Pennsylvania, Civil Action No. 97-3820, Expert report in February, 1998; on behalf of U.S. Department of Justice.

Declaration before the Federal Communication Commission, CC Docket No. 97-211, in the Matter of Applications of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications to WorldCom, Inc., January 25, 1998 (with Dennis Carlton); on behalf of WorldCom and MCI.

Smith v. Amtrak, Circuit Court of Cook County, IL, Case 92 L 10525. Deposition in November 1997, trial testimony in January 1998; on behalf of Smith.

Johnson and Lehl v. City Colleges of Chicago, U.S. District Court for the Northern District of Illinois Eastern Division Case No. 96 C 0862. Expert report in July 1997, deposition testimony in November 1997; on behalf of City Colleges of Chicago.

Gelumbauskas v. Precision Gear, U.S. District Court, Northern District of Illinois Eastern Division, Case No. 96 C 0862. Expert report in April 1997; on behalf of Gelumbauskas.

Galvan v. U.S. Industries, Expert Report on December 27, 1997, deposition testimony in January 1997; on behalf of U.S. Industries.

Sprint Communications Company L.P. v. Network 2000 Communications Corporation, Expert report on July 15, 1996, deposition testimony in July, August 1996; affidavit on November 9, 1996; on behalf of Sprint.

Beazer East v. CSX Transportation, Inc., U.S. District Court for the Western District of Pennsylvania Case No. 93 0861, Expert report in April 1996; deposition testimony in June 1996; on behalf of CSX.

Report submitted in May 1996 to the National Association of Insurance Commissions on behalf of National Association of Independent Insurers.

Carbon Dioxide Industry Litigation, U.S. District Court for Central District of Florida MDL940. Expert report in October 1994 (with William M. Landes); supplemental report (with William M. Landes and Richard Leftwich) in May 1995; deposition testimony in July 1995; on behalf of opt-out plaintiffs.

AVR, Inc. v. Cemstone Products Corp., U.S. District Court, District of Minnesota, Third Division, File CIV 3-92-551. Expert report in October 1994; supplemental affidavits in December 1994, January 1995; on behalf of Cemstone.

W. Borysiewicz v. M. Gilblair, Circuit Court of Cook County, Illinois. Deposition testimony in August 1994; trial testimony in September 1994; on behalf of Borysiewicz.

NAACP et. al. v. American Family Mutual Insurance Co., U.S. District Court, Eastern District of Wisconsin, Civil Action No. 90-C-0759. Deposition testimony in July 1994 and November 1994; on behalf of American Family.

G. Bowan v. The Sales Force Companies, U.S. District Court for The Western District of Missouri, Case No. 92-0496-CV-W-2. Affidavit in February 1993; on behalf of Sales Force.

Wisconsin Central Transportation Corporation -- Continuance in Control -- Fox Valley and Western Ltd., Finance Docket 32036. Verified Statement to the Interstate Commerce Commission in September 1992 (with Andrew M. Rosenfield); on behalf of the Wisconsin Central.

Castaneda v. Baron Wire and Steel Inc., Circuit Court of Cook County, Illinois, Municipal Department, Second District. Deposition testimony in February 1992; on behalf of Castaneda.

Morgan v. ServiceMaster, U.S. District Court for the Northern District of Illinois, Case No. 89-C-0581. Report in August 1991 (with Sherwin Rosen); on behalf of ServiceMaster.

Sepich v. Mueller, U.S. District Court for the Central District of Illinois, U.S. District Court, Case No. 88-2353. Report in March 1991 (with Sherwin Rosen); on behalf of Mueller.

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Times Herald Printing Company v. A.H. Belo Corp. and Dallas Morning News Company, District Court of Harris County Texas, 280th Judicial District. Deposition testimony in April 1990; on behalf of Dallas Morning News.

Turner v. IDS Financial Services, Inc., U.S. District Court for the District of Minnesota, File No. 88-521. Report in November 1989; on behalf of IDS.

McLendon et al. v. Continental Group et. al, U.S. District Court for the District of New Jersey, Civil Action No. 83-1340 (SA). Trial testimony in February 1989, testimony before Special Master in February 1990; testimony before Special Master (with Sherwin Rosen) in August 1990; on behalf of Continental Group.

Application of Illini Carrier L.P. before Illinois Commerce Commission. Testimony in April 1988 regarding application to provide natural gas transportation services; on behalf of Illini Carrier.

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EDUCATION

Ph.D. UNIVERSITY OF CHICAGO: Economics, 1996
(Full scholarship from the University)

M.A. UNIVERSITY OF CHICAGO: Economics, 1993
(Full scholarship from the University)

B.S. SOUTHERN METHODIST UNIVERSITY: Economics and Systems Analysis,
Mathematics Minor, 1991
(Summa Cum Laude, Honors, Departmental Distinction)

EMPLOYMENT

LEXECON, INC., Chicago, Illinois: Economist (1996 - present)

UNIVERSITY OF CHICAGO: Teaching Assistant (1994 - 1996)

DEGOLYER SPECIAL COLLECTIONS LIBRARY (May - July 1991)

BARNES & NOBLE (May - July 1989)

UNIVERSITY OF TEXAS, Research Assistant to Dr. Brian Berry (May - July 1987)

OTHER PROFESSIONAL EXPERIENCE

Member of the *American Economics Association*

Associate member of the *American Bar Association*

Referee for the *American Journal of Agricultural Economics* and *Journal of Business*.

Coordinated the *Conference on Valuing Non-Market Goods*, University of Chicago (July 21-22, 1995)

Assisted in coordinating the *Conference on Research in Health Economics*, University of Chicago (October 21-22, 1994)

Assisted in organizing the *Economic Policy and Public Finance Workshop*, University of Chicago (1993 - 1996)

Presented papers on information externalities and technology diffusion at the *Economics and Public Policy Workshop* (3) and *Price Theory Workshop* (1), University of Chicago (1995, 1996)

Presented *The Impact of Technology on the Modern Labor Market* at the 68th Annual Meeting of the Southwestern Social Science Association (March 29, 1990)

Independent research projects with Drs. Slottje and Hayes, Southern Methodist University (1987 - 1991)

ACADEMIC HONORS

Graduated Summa Cum Laude, Honors, Department Distinction

Phi Beta Kappa

Alpha Lambda Delta (Treasurer, honorary society recognizing academic achievement)

Phi Eta Sigma (honorary society recognizing academic achievement)

Omicron Delta Epsilon (international honor society in economics)

Kappa Mu Epsilon (honor society in mathematics)

Award for Excellence (given to the outstanding senior in the Economics Department as decided by the vote of the faculty)

Presidential Scholarship (full scholarship, Southern Methodist University)

National Merit Scholar (honorary)

Full Scholarship (University of Chicago)

Hyer Society (honorary society of Southern Methodist University)

Honor Roll (1987-1991)

AREAS OF SPECIALIZATION

Telecommunications

Technology Diffusion

Urban Economics

Agricultural Economics

Environmental Economics

PUBLICATIONS

BOOKS

Down to the Wire: Studies in the Diffusion and Regulation of Telecommunications Technologies, (Editor) Nova Science Press (forthcoming 2003).

ARTICLES

"The Evolution of Telecommunications Switching in the Central Office," in Down to the Wire: Studies in the Diffusion and Regulation of Telecommunications Technologies, Nova Science Press (forthcoming 2003).

Handicapping Countries in the Race to Digital Switching, Progress in Economics, edited by Frank Columbus (forthcoming 2003).

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Determinants of the Diffusion of U.S. Digital Telecommunications, Journal of Evolutionary Economics, 11 (2001).

Compensating for Information Externalities in Technology Diffusion Models, 80 American Journal of Agricultural Economics, 2 (1998).

Contributed to two catalogs at DeGolyer Special Collections Library (1991).

The Impact of Technology on the Modern Labor Market, 11 Southwestern Journal of Economic Abstracts, 1 (1990).

RESEARCH PAPERS

An Evaluation of Technology Diffusion Models and Their Implications, Ph.D. Dissertation, University of Chicago (1996).

A New Direction in Mixed Income Housing, submitted to Chicago Housing Authority (1993).

UNPUBLISHED PAPERS

A Survey of the Economics of Information, Focussing on Water (1992).

Petroleum Price Shocks and Rationality, B.S. Honors Paper (1991).

EXPERT TESTIMONY

Reply Declaration Re: 2000 Biennial Regulatory Review Spectrum Aggregation Limits for Commercial Mobile Radio Services, Before the Federal Communications Commission, Washington DC, WT Docket No. 01-14, May 14, 2001, Reply Declaration (with Robert Gertner).

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Report to Directorate General IV of the European Commission: "Remedies in the United States," in *Remedies in the United States*, in *Remedies in EU Competition Law: The Policy and Practice of the European Commission, A Report for Directorate General IV of the European Commission*, July 1998, Report (with James Langenfeld).

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of)	
)	
Section 272(f)(1) Sunset of the BOC Separate)	WC Docket No. 02-112
Affiliate and Related Requirements)	
)	
2000 Biennial Regulatory Review)	CC Docket No. 00-175
Separate Affiliate Requirements of Section)	
64.1903 of the Commission's Rules)	

QWEST REPLY COMMENTS

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July 28, 2003

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.**

In the Matter of

**Section 272(f)(1) Sunset of the BOC Separate
Affiliate and Related Requirements**

**2000 Biennial Regulatory Review
Separate Affiliate Requirements of Section
64.1903 of the Commission's Rules**

WC Docket No. 02-112

CC Docket No. 00-175

**REPLY DECLARATION OF
DENNIS W. CARLTON, HAL SIDER AND ALLAN SHAMPINE**

July 28, 2003

I. INTRODUCTION AND SUMMARY

1. We submitted a declaration in this matter on June 30, 2003 that presented the bases for our conclusion that elimination of structural separation requirements preventing ILECs from fully integrating their long-distance and local exchange operations will not adversely affect long-distance competition. Our analysis indicated that there is no economic basis for subjecting BOCs' in-region long-distance service to dominant carrier regulation following the sunset of Section 272 structural separation requirements, nor is there any economic basis for conditioning the non-dominant status of independent LECs' long-distance operations on the structural separation of those operations. Our June 30 declaration contains a summary of our qualifications.

2. At the request of counsel for Qwest, Verizon and SBC, we address certain points raised in comments submitted by other parties in this matter. Our reply focuses on comments by AT&T and the supporting affidavit by Dr. Lee L. Selwyn, which support the imposition of dominant carrier regulation on ILEC-provided long-distance services. Many of the points raised by AT&T and Dr. Selwyn are representative of issues raised in other parties' comments. We focus on issues they raise that were not directly addressed in our June 30 declaration. Our failure to discuss the remaining claims made by AT&T or Dr. Selwyn should not be interpreted to suggest that we agree with their analysis or conclusion.

3. The FCC's Further Notice of Proposed Rulemaking (FNPRM) asked whether elimination of structural separation requirements would be likely to: (i) facilitate non-price discrimination by ILECs against their long-distance rivals; (ii) facilitate a predatory price squeeze by ILECs against their long-distance rivals; and/or (iii) enable ILECs to shift costs from long-distance to local operations in a manner that would adversely affect long-distance

competition. The FNPRM also inquired whether dominant carrier regulation would address these potential concerns.

4. Our prior declaration described the conditions under which such strategies might succeed and showed that such conditions do not exist in the long-distance industry. AT&T and Dr. Selwyn have not shown otherwise.

- Successful non-price discrimination in degrading access to rival long-distance carriers requires both that ILECs' efforts not be detected by regulators and rival long-distance providers and that they be sufficient to induce consumers to switch to ILEC-provided services. AT&T and Dr. Selwyn fail to establish that (i) these unlikely circumstances both occur; (ii) elimination of structural separation requirements facilitates the pursuit of non-price discrimination by ILECs; and (iii) imposition of dominant firm regulation would be a necessary or appropriate way to address this risk.
- Successful pursuit by ILECs of a predatory price squeeze against rival long-distance providers would require that ILECs set long-distance prices at a sufficiently low rate and for a sufficiently long time to drive their rivals from the industry. Successful predation also requires that these rivals not reenter the industry (and that others not enter) since such entry would prevent ILECs from recouping their investment in predation through higher prices. Our prior declaration explained that successful predation is rare and AT&T and Dr. Selwyn fail to establish that there are any realistic predation concerns in the long-distance industry, especially given the ability of consumers to use wireless services to make long-distance calls, or other alternatives such as e-mail, instant messaging and voice over IP. They further fail to show that imposition of dominant carrier

regulation is a necessary or appropriate way of preventing such an unlikely occurrence.

- With respect to potential concerns that cost shifting by ILECs from unregulated to regulated activities could adversely affect long-distance competition, AT&T and Dr. Selwyn fail to establish that an ILEC's ability to predate depends in any way on its ability to shift costs. As discussed in our prior declaration, if an ILEC could predate – and there is no evidence suggesting that this is a realistic possibility – its ability to do so would not depend on its ability to shift costs. Neither do AT&T or Dr. Selwyn establish that (i) cost shifting that does not result in predation adversely affects long-distance competition in any way, or (ii) dominant firm regulation is a necessary or appropriate way of addressing the matter. As we discussed in our prior declaration, there is little if any incentive for integrated carriers to shift costs because regulated rates for local services are largely set independently of the costs reported by ILECs due to price caps and other forms of incentive regulation.

II. ILECS HAVE NO INCENTIVE TO SET LONG-RUN PRICES FOR LONG-DISTANCE SERVICES AT A LEVEL THAT DRIVES EFFICIENT RIVALS FROM THE INDUSTRY OR TO ENGAGE IN PREDATION

A. ILECS HAVE NO INCENTIVE TO SET LONG-RUN PRICES THAT RESULT IN THE EXIT OF EFFICIENT RIVALS EVEN IF ACCESS CHARGES EXCEED ILECS' COST OF PROVIDING ACCESS

5. AT&T's comments suggest that ILECs have a long-run incentive to set prices below competitive levels and, as a result, drive even efficient long-distance rivals from the long-distance industry. Its arguments focus on its claim that the cost to ILECs of providing access is

below the access charge to long-distance carriers.¹ This concern is further reflected in AT&T's longer-term policy goals, which are described in Section IV of its comments:

There is a critical need for comprehensive intercarrier compensation reform in order to remove the BOC access cost advantage resulting from the current system of above-cost interstate and intrastate switched access rates, and to reduce the BOCs' ability and incentives to engage in anticompetitive price squeezes, and other anticompetitive cross-subsidization.²

6. There is no basis to AT&T's claim. AT&T ignores the fact that ILECs lose access revenue when they provide long-distance services. That is, when ILECs provide long-distance service they gain retail revenue but lose access revenue paid by a subscriber's prior long-distance carrier. The loss in access revenue is a real cost of providing retail long-distance service faced by ILECs which must be considered in any evaluation of the prices charged by ILECs as long-distance carriers.

7. For example, assume that the cost to an ILEC of providing access to long-distance carriers (including itself) is zero but long-distance carriers face access charges of \$.01 per minute.³ If an ILEC, rather than an independent long-distance carrier, provides long-distance service through its own affiliate at the retail price of \$.05 per minute, it gains retail revenue of \$.05 per minute but loses access revenue of \$.01 per minute that it otherwise would have earned. In deciding whether to provide, and how to price, long-distance service, the ILEC must take into account the potential loss of access revenue. Any such loss in access revenues from long-

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1. For the purpose of this discussion, we assume that AT&T's claim that access charges are above ILECs' cost of providing access is correct and show that AT&T's argument fails nonetheless. Regardless of whether AT&T's assumption has merit, the fact that the Commission regulates access prices indicates that it believes that such regulation typically results in prices lower than would otherwise occur.
 2. Comments of AT&T Corp., p.68 (hereafter, AT&T Comments).
 3. We recognize that there is a cost of providing access, but for simplicity we assume zero cost in this example. The conclusions in this section are not altered if a non-zero cost is assumed.

distance carriers is a real cost (which economists call an "opportunity cost"). In our example, the ILEC would profitably provide long-distance service if the additional \$.04 it earns by providing retail service (instead of access service alone) more than offsets the additional costs that it incurs in providing retail long-distance service. We refer to this \$.04 as the "retail margin."

8. Thus, the access charge of \$.01 represents a \$.01 opportunity cost faced by the ILEC when it induces a long-distance customer to switch to its own long-distance service for a call. The effective margin earned by the ILEC in providing retail long-distance service (instead of access alone) is only \$.04 per minute, the same net-of-access-cost margin the long-distance carrier earns (assuming it charges the same retail price). Thus, even if ILECs face costs of providing access that are less than the access charges paid by rival long-distance carriers, they have no long-run incentive to set price below \$.05 per minute, the level implied by their opportunity cost of access and other relevant costs of efficiently providing long-distance service. At any lower price, ILECs would fail to earn a price that covers all their relevant costs.

9. This logic implies that ILECs will not have an incentive to provide long-distance service if rival carriers are more efficient. For example, assume that an efficient long-distance carrier requires a retail margin (retail long-distance price minus access charges) of \$.04 to cover its relevant costs to provide long-distance service, while the ILEC requires a minimum retail margin of \$.05 (ignoring the access charges) to provide long-distance service. (Recall that, for simplicity's sake, we assume above that ILECs can provide access at zero cost.) The ILEC's higher costs may, for example, reflect the fact that its network is less efficient than the networks of other long-distance carriers.⁴ In this example, the long-distance carrier would, by assumption,

4. Betsy Barnard, President of AT&T noted, "We have a significant advantage against any of the Bells... They don't have the assets, the networks, the services. It takes decades to build that capability." (Reinhardt Kraus, "Bernard Faces New Round of Challenges," Investor's

just cover its relevant costs of providing long-distance service (i.e., revenue of \$.05 minus access charges of \$.01 equals the required \$.04 needed to cover relevant costs). The ILEC, however, would not cover its relevant costs including the opportunity cost of lost access fees if it provided the long-distance service instead (i.e., \$.05 minus the opportunity cost of \$.01 fails to cover the \$.05 needed to cover the ILEC's relevant costs). Hence, the ILEC earns greater profits if its rivals provide long-distance service rather than itself (another way to establish this point is as follows: if rival long-distance carriers provide service, the ILEC earns \$.01 in access charges, while if the ILEC provides the long-distance service itself, it earns nothing). As this example indicates, ILECs have no incentive to set the long-run price of long-distance service below the level implied by access charges and a competitive retail margin, and thus no incentive to drive more efficient long-distance rivals from the industry.⁵

10. For simplicity, the above discussion does not account for the expansion in output expected if long-distance prices were to fall below \$.05.⁶ This simplification, however, does not alter the basic conclusion that ILECs have no incentive to lower long-distance prices below the long-run competitive level (i.e., the level at which revenues cover relevant costs) and drive more efficient rivals from the industry in order to provide long-distance themselves. To see this point, assume that long-distance is competitive (in the sense that retail prices exceed access costs by an

(...continued)

Business Daily, July 21, 2003.)

5. Consumers would benefit if ILECs were to attempt to set prices below the long-run competitive level (\$.05 per minute) as long as this investment could not be recouped by raising prices above the competitive level in the longer term. As discussed in our initial declaration and further below, it is highly unlikely that such recoupment would be possible in the long-distance industry.
6. The FCC raises this as a potential issue in its Opinion in the Matter of Regulating Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace, 12 FCC Rcd 15,756 (1997), ¶127 (hereafter, LEC Non-Dominance Order).

amount sufficient to enable long-distance carriers to earn only a competitive rate of return). Under these circumstances, if a reduction in access charges (and thus a reduction in retail rates) generated higher total access revenues as a result of higher usage, then ILECs would be expected to voluntarily reduce access charges, regardless of whether they also offer long-distance services. Because the FCC and states generally regulate the price of access (except for special access in areas where there is facilities-based competition), and long-distance carriers advocate such regulation, the FCC and long-distance carriers must believe that ILECs would increase access rates in the absence of regulation. (That is, if ILECs were not constrained by regulation, their profit-maximizing strategy would be to increase access fees, not to decrease them.) If that is so, ILECs would lose money by decreasing the price of access. Thus, there is no reason to expect that ILECs would set long-run prices below the level implied by access charges plus a competitive retail margin in order to drive more efficient long-distance rivals from the industry, even if output would expand at prices below \$.05.

11. As this indicates, AT&T and Dr. Selwyn have not correctly identified the costs faced by ILECs in providing retail long-distance service. ILECs have no incentive to lower the long-run prices of long-distance services below the level implied by access charges and a competitive retail margin in order to provide the services themselves. As such, the success of long-distance carriers and ILECs in providing long-distance service will depend on which is more efficient.

B. ILECS DO NOT HAVE THE INCENTIVE OR ABILITY TO ENGAGE IN A PREDATORY PRICE SQUEEZE, EVEN IF ACCESS CHARGES EXCEED ILECS' COSTS OF PROVIDING ACCESS

12. Based on the mischaracterization of the effective costs faced by ILECs in providing long-distance services described above, AT&T and Dr. Selwyn argue that ILECs have the incentive and ability to engage in predatory price squeezes by setting retail long-distance

prices at or near access charges faced by their long-distance rivals.⁷ This argument has no merit since above-cost access prices do not facilitate predation and cost-based access prices do not (by themselves) preclude predation.

13. As suggested above, regulated prices that long-distance carriers pay to access ILEC networks are one determinant of the retail price of long-distance services. Higher access charges result in higher costs to long-distance carriers and higher opportunity costs to ILECs when providing retail long-distance services, and thus higher long-distance prices charged by both ILECs and their rival carriers.

14. The level of the access charges faced by non-ILECs for originating and terminating calls does not affect an ILEC's incentive or ability to engage in a predatory price squeeze.⁸ A predatory price squeeze requires that the ILEC charge a price below its rivals' costs (which include both access charges and any other relevant costs an efficient long-distance provider would face in providing service). An ILEC that pursues a predatory price squeeze "invests" by setting retail long-distance prices at below-cost levels (where costs reflect both access charges and other costs of providing long-distance service). Its low retail prices result in both a reduction in the ILEC's retail revenues (from existing retail customers) and its access revenues from other long-distance carriers when customers switch from rivals' long-distance services to its own.

7. As summarized in the AT&T Comments (pp. 30-31), "[t]he BOCs also are using their special access bottlenecks to price squeeze IXC competitors ... by raising the price of special access services to all interexchange carriers, thus causing competing IXCs ... 'to either raise their retail rates ... or ... reducing their profit margin'." Also see AT&T Comments (p. 26).

8. This discussion treats long-distance as a single service. In fact, long-distance includes a variety of services such as interstate and intrastate long-distance. As discussed below, predation requires that prices be set below relevant costs for all services taken as a whole in order to drive rivals from the industry.

15. The fact that an ILEC might appear still to earn a positive accounting margin (defined as revenue less costs, ignoring lost access fees) by setting price below access charges is not relevant for evaluating whether predation makes economic sense. Even if the ILEC earned a positive accounting margin during a predatory price squeeze, it still must bear the cost of lost retail revenue and access revenue. Any attempt to engage in a predatory price squeeze also would likely require that retail prices be set below the appropriate measure of costs for an extended period of time. This in turn suggests that the "victims" of this strategy would have the opportunity to pursue complaints about such conduct, which further reduces the likelihood that such efforts could succeed.

16. For an ILEC to recoup its investment in predation, it would have to raise retail prices above the preexisting levels after rivals are driven from the industry. As discussed in our prior declaration, it is highly unlikely that a long-distance carrier could recoup any investment in predation due to the difficulty of precluding competition if prices were to rise above preexisting levels.

- Provision of long-distance service involves extensive use of fixed assets that would remain in the industry even if a service carrier became bankrupt. These assets would be available (probably at a fraction of their original cost) to any entrant and/or to firms that would emerge from bankruptcy proceedings resulting from below-cost pricing, as would the human capital (the workers) formerly employed by the bankrupt firm.
- In addition, the widespread use of wireless services for long-distance calling (as well as e-mail as a substitute for certain long-distance calls) adversely affects an ILEC's ability to recoup an investment in predation by raising long-distance price

after driving its rivals from the industry because certain calls will be lost to these other modes of communication.

- Successful recoupment subsequent to predation would be easily detectable and would likely trigger a regulatory response.

17. In sum, the level of access charges is irrelevant to an ILEC's ability to pursue a predatory price squeeze. This strategy is deterred by the difficulty the ILEC would face in recouping its investment in predation, not by the relationship between access charges and access costs (even if parties could agree on the correct measure of cost).

C. PER MINUTE CHARGES FOR INTRASTATE LONG-DISTANCE CALLS NEAR OR BELOW ACCESS CHARGES ARE NOT EVIDENCE OF A PREDATORY PRICE SQUEEZE

18. AT&T and Dr. Selwyn claim that BOCs are currently engaging in predatory price squeezes against their long-distance rivals. For example, AT&T claims that "BOCs are engaging in price squeezes by setting their long-distance rates at or below their switched access prices."⁹ Citing Dr. Selwyn's declaration, AT&T claims that BOCs offer long-distance calling plans at rates equal to or below intrastate access prices in Texas, Virginia and Washington.¹⁰

19. The examples presented by AT&T and Dr. Selwyn, however, do not support their claims that BOCs are engaging in predatory price squeezes against their long-distance rivals.¹¹ A predatory price squeeze drives rival long-distance suppliers out of business. But if rivals provide many services (such as interstate and intrastate long-distance), predation can succeed only if the target firms are driven from the industry (i.e., if their total revenue fails to cover the total non-

9. AT&T Comments, p. 26.

10. AT&T Comments, p. 27 citing Declaration of Lee L. Selwyn on behalf of AT&T, June 30, 2003, ¶¶43-48, 84-88, 96 (hereafter, Selwyn Declaration).

11. Curiously, Dr. Selwyn focuses on intrastate rates even though this inquiry deals with interstate rates.

sunk costs of long-distance service). More specifically, even if access prices exceed the per-minute component of price for some retail calls, this would not prove predation.

20. Long-distance services include a variety of types of calls including interstate/interLATA calls, intrastate/interLATA calls, and international calls to various destinations. Different types of calls may result in different costs to long-distance carriers. For example, access charges for intrastate calls vary across states and often differ from access charges for interstate calls. Long-distance carriers also may face higher costs for completing calls that travel longer distances.¹²

21. When firms offer a variety of diverse services, there are a variety of prices they can charge that enable them to cover costs. With respect to long-distance services, firms may well earn the same net-of-access-cost margin for interstate and intrastate calls (by charging different prices for these types of calls when access charges differ). Other carriers may choose to charge the same per-minute price for interstate and intrastate long-distance calls and earn different margins on each.

22. Presumably, long-distance carriers choose price schedules for different types of calls based on a variety of considerations including cost differences for different types of calls, the mix of calls made by their subscribers, and marketing considerations. For example, a long-distance carrier may determine that charging the same rate for interstate and intrastate long-distance calls may help attract customers.¹³

12. For example, calls that cover longer distances occupy greater network capacity than calls that cover shorter distances.

13. We understand that if a company offers a plan that does not differentiate between interstate and intrastate long-distance, it is required to offer the same plan on the same terms in all states, even though intrastate access fees and other costs differ between states. Under Dr. Selwyn's theory, the company would be pricing predatorily if the per-minute charges were lower than the highest access cost in any state.

23. Under these circumstances it is not surprising that different firms adopt different pricing schedules. For example, some long-distance carriers charge the same per-minute rates for interstate and intrastate long-distance calls even when access fees differ.¹⁴ Similarly, some plans charge more for calls that cover greater distance (within the U.S. mainland) while other plans do not.¹⁵ The relevant question for evaluating predation, however, is whether revenue for all services taken as a whole exceeds the relevant costs in providing all services.

24. More generally, "below-cost" pricing for only one of multiple dimensions of service (e.g., intrastate long-distance calls in one state) does not imply that a firm is engaged in predation. Instead, predation requires first that prices be set at a sufficiently low level that rival firms are driven from the industry. This requires analysis of whether the revenue for all services taken as a whole exceeds the relevant costs incurred in providing those services. While Dr. Selwyn claims that per-minute charges below access rates for intrastate calls alone reflect an anticompetitive price squeeze, he is wrong. As he acknowledges in other parts of his analysis, it is inappropriate to consider interstate and intrastate interLATA calls as separate services.¹⁶

25. Similarly, since the mix of services consumed by different customers will vary, there may be differences in the profitability of serving different customers when the margins for each of the individual services in the package differ. However, the profitability of any given customer is not relevant for analyzing predation, which again requires that prices be set

14. For example, AT&T's "One Rate USA" and "Unlimited" plans charge the same per-minute fees for intrastate and interstate calls, while its "5 cent nights" and "5 cent weekend" plans do not.

15. See, for example, Sprint's "Dial 1" and "The Most II" services.

16. Selwyn Declaration, pp. 37-38, states: "Customers cannot and do not make separate service provider selections *notwithstanding the fact that the two services are subject to different regulatory treatment by different regulatory authorities and may be offered at different prices.*" (Emphasis in original.)